TITLE 17: CALIFORNIA AIR RESOURCES BOARD

NOTICE OF PUBLIC HEARING TO CONSIDER AMENDMENTS TO THE CALIFORNIA CAP ON GREENHOUSE GAS EMISSIONS AND MARKET-BASED COMPLIANCE MECHANISMS

The Air Resources Board (ARB or Board) will conduct a public hearing at the time and place noted below to consider proposed amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms to: allow for additional transition assistance for covered entities, add a new offset protocol, and incorporate additional cost containment features.

DATE: October 24, 2013
TIME: 9:00 a.m.
PLACE: California Environmental Protection Agency
Air Resources Board
Byron Sher Auditorium
1001 I Street
Sacramento, California 95814

WEBCAST: http://www.calepa.ca.gov/broadcast/?BDO=1

This item may be considered at a two-day meeting of the Board, which will commence at 9:00 a.m. October 24, 2013, and may continue at 8:30 a.m. on October 25, 2013. This item may not be considered until October 25, 2013. Please consult the agenda for the hearing, which will be available at least 10 days before October 25, 2013, to determine the day on which this item will be considered.

INFORMATIVE DIGEST OF PROPOSED ACTION AND POLICY STATEMENT
OVERVIEW PURSUANT TO GOVERNMENT CODE 11346.5(a)(3)

Sections Affected: Proposed amendments to sections 95802, 95811, 95812, 95813, 95814, 95821, 95830, 95831, 95832, 95833, 95834, 95841.1, 95851, 95852, 95852.1.1, 95852.2., 95853, 95856, 95857, 95870, 95890, 95891, 95892, 95893, 95910, 95911, 95912, 95913, 95914, 95920, 95921, 95922, 95942, 95970, 95971, 95972, 95973, 95974, 95975, 95976, 95977, 95977.1, 95978, 95979, 95980, 95980.1,95981, 95981.1, 95982, 95983, 95984, 95985, 95986, 95987, 95990, and 96022, title 17, California Code of Regulations. Proposed adoption of new sections 95894, 95895, 95923, 95979.1, Appendix B, and Appendix C, title 17, California Code of Regulations. Proposed adoption of the incorporated California Air

Documents Incorporated by Reference:

The following documents are hereby proposed for incorporation by reference by ARB into the Staff Report for the proposed amendments to the regulation and the proposed Compliance Offset Protocol:


https://www.sce.com/wps/wcm/connect/d63903ad-925d-4a1c-a2b5-62c261a3a82c/CPUC_D_1012035.pdf?MOD=AJPERES


**Background and Effect of the Proposed Rulemaking**

The California Global Warming Solutions Act of 2006 (Assembly Bill 32; Stats. 2006, Chapter 488) (AB 32) authorizes ARB to implement a comprehensive, multi-year program to reduce greenhouse gas (GHG) emissions in California. AB 32 required ARB to develop a scoping plan to reduce GHG emissions in California to 1990 levels by 2020. ARB’s adopted Scoping Plan includes a comprehensive set of actions designed to reduce GHG emissions in California, improve the environment, reduce dependence on foreign oil, diversify energy sources, save energy, create new jobs, and enhance public health. Meeting the goals of AB 32 requires a coordinated set of strategies to reduce GHG emissions throughout the economy that work within a comprehensive tracking, reporting, verification and enforcement framework. The Scoping Plan includes a variety of measures to achieve AB 32 goals, including direct regulations, performance-based standards, and market-based mechanisms. Many of the measures in the Scoping Plan complement and reinforce each other.

The Scoping Plan identified a cap-and-trade regulation (Regulation) as one of the most important strategies for achieving emissions reductions at least cost. As envisioned in the Scoping Plan, the cap and trade program would eventually be linked with cap and trade programs operating in other states and provinces. The Regulation provides a fixed limit on GHG emissions from the sources responsible for about 85 percent of the State’s total GHG emissions. The Regulation reduces GHG emissions by applying a declining aggregate cap on GHG emissions, and creates a flexible compliance system through the use of tradable instruments (allowances and offset credits). The Regulation is designed to link with partners in other jurisdictions. The California Cap-and-Trade Regulation went into effect January 1, 2012.

In 2012, ARB staff proposed two sets of amendments to the Regulation. The first set was focused on implementation requirements and the second on linking the California and Québec cap-and-trade programs. At its June 2012 Board hearing, the Board
approved the implementation amendments, which became effective September 1, 2012. At its April 2013 Board hearing, the Board approved the linkage amendments. The linkage amendments become effective October 1, 2013, with a linked California and Québec cap-and-trade program effective on January 1, 2014.

In developing the proposed amendments described in this notice, staff held nine workshops and released discussion draft regulation amendments for public comment. ARB received more than 75 written comments on the discussion draft amendments and met regularly with stakeholders to discuss concerns and recommendations. The proposed amendments provide additional process for clarity in implementation, address stakeholder concerns on cost containment, add a new compliance offset protocol, and extend transition assistance for covered entities in the program. In a separate rulemaking action, ARB is amending its mandatory reporting regulation to support some of these proposed changes to the cap-and-trade program.

**Objectives and Benefits**

The purpose of these amendments is to enhance implementation and oversight of the Cap-and-Trade Program. The proposed amendments also address stakeholder concerns related to cost containment and offset supply. To that effect, staff is proposing amendments to the Regulation, including those related to allocation, market program implementation, and offset program implementation. Staff has proposed allocation for additional sectors, changes to allocation methodologies, and changes to transition assistance for existing sectors. Proposed amendments for market provisions relate to implementation, auctions and reserve sales, additional information reporting, cost containment, and enhancements to support market oversight. Staff has also proposed clarifications and new provisions to help implement the offset program. Staff has proposed amendments that will shift the scheduled reduction in allowance allocation assistance factors by one compliance period. This shift is intended to provide additional time and certainty to industry in making necessary investments in efficiency and emission reducing technologies. Details regarding the proposed amendments are included in Chapter II: Summary of Proposed Action and in Appendix A of the Staff Report. Staff is also proposing a new protocol related to mine methane capture that will provide additional supply of compliance instruments to the market within the existing 8 percent offset limit.

Anticipated benefits of the proposed amendments include improved clarity for covered entities regarding the allocation of emission allowances, timelines for compliance, offset program implementation and verification, cost containment, enhanced market monitoring and program oversight, and clarity in the emissions reductions required by the program. Given the GHG emissions reductions which will occur because of the
program, these amendments may also directly improve the health and welfare of California residents, worker safety, and the State’s environment. Specific discussion of the proposed amendments follows.

**Resource Shuffling**

Per Board Resolution 12-33, the Board directed staff to continue to work with the Emissions Markets Advisory Committee (EMAC), the California Independent System Operator (CAISO), State agencies and stakeholders to provide certainty to the electricity market about how the Regulation will address resource shuffling. The Board also directed staff to further refine the definition of resource shuffling and to identify situations that ARB would not consider resource shuffling. Recommended actions were presented to the Board at the October 2012 Board meeting. Based on these recommended actions, staff developed guidance for the definition of resource shuffling, and identified “safe harbors,” or activities that covered entities may engage in that ARB does not consider resource shuffling. Staff has proposed clarifying amendments to the Regulation consistent with the previously recommended actions and published guidance regarding the definition of resource shuffling and the identified safe harbors.

**Legacy Contracts**

Per Board Resolution 12-33, the Board directed staff, in coordination with the California Public Utilities Commissions (CPUC), to develop a methodology that provides transition assistance to covered entities that have a compliance obligation cost that cannot be reasonably recovered due to a legacy contract. Staff evaluated existing legacy contract issues and has proposed methodologies to be included in the Regulation that provide transition assistance through free allocation of allowances to those covered entities with legacy contracts, and through changed allocation of allowances to legacy contract counterparties.

**Combined Heat and Power**

Per Board Resolution 12-33, the Board directed staff to work with the CPUC, the California Energy Commission (CEC), and stakeholders to develop a methodology that exempts the steam and waste heat emissions for all facilities that would not be included in the Cap-and-Trade program “but for” their investment in combined heat and power (CHP). Staff has proposed a methodology and regulatory language that provides for a process to quantify emissions eligible for the exemption and to retire equivalent allowances in order to maintain the environmental integrity of the Program.
Emissions Leakage

Per Board Resolutions 12-33 and 11-32, the Board directed staff to continue to evaluate trade exposure categorization and, if necessary, modify the leakage risk determinations to be implemented prior to the allocation of allowances for the second compliance period. The Board further directed staff to complete current studies of leakage risk and evaluate options for ensuring the competitiveness of California industries. Staff has proposed new and modified leakage risk determinations based on the status of current studies under contract to ARB. In addition, staff proposed to increase the assistance factor to 100% throughout the second compliance period for those sectors defined at medium- and low-leakage risk. The third compliance period assistance factor was increased to match the previous assistance factor for the second compliance period for each the respective sector. This change was in recognition of the need for regulatory certainty for businesses while the new leakage studies are completed.

Universities

Per Board Resolution 12-33, the Board directed staff to develop a methodology to allocate allowances to California universities that recognizes early actions by universities to reduce greenhouse gas (GHG) emissions, and invest in energy efficiency and CHP. Staff has proposed a methodology for the direct allocation of allowances to California universities that are covered entities as a result of early action GHG reduction activities.

Offset Program Implementation

Staff has evaluated and proposed amendments which clarify processes related to offset program implementation. These amendments address project listing requirements, monitoring and reporting requirements, verification body requirements, conflict of interest requirements, compliance offset credit issuance, timing and deadlines, and roles of air districts. Staff has also proposed changes to clarify the invalidation requirements to be consistent for all project types.

Cost Containment

Per Board Resolution 12-51, staff has proposed amendments to further ensure that allowance prices will not exceed the highest price tier of the Allowance Price Containment Reserve while minimizing the impact on existing allowances and maintaining the environmental integrity of the Program.
Product-Based Benchmarks

Per Board Resolution 11-32, the Board directed staff to identify and propose new benchmarks and allowance allocation for manufacturing of new products in California. Staff is proposing new product benchmarks for various sectors, including those sectors for which data was not previously collected through the Regulation for the Mandatory Reporting of Greenhouse Gas Emissions (title 17, California Code of Regulations, section 95100 et seq.), but which may be eligible for free allocation and for activities currently under the energy-based methodology of allowance allocation. Staff has also proposed changes to certain existing benchmarks based on newly available data, where appropriate.

Allowance Allocation

Per Board Resolution 11-32, the Board directed staff to continue to work with stakeholders to further develop the allowance allocation approach for the petroleum refining sector in the second and third compliance period. Staff is proposing modifications to the true-up methodology and considering changes to the allocation methodology associated with refinery allowance allocation using a carbon weighted approach. Staff is also proposing an allocation methodology for suppliers of natural gas, which will have a compliance obligation beginning with the second compliance period. Finally, staff is proposing an allocation methodology for public wholesale water agencies for the protection of water ratepayers.

Waste-to-Energy

Per Board Resolution 12-33, the Board directed staff to develop regulatory amendments to exempt waste-to-energy facilities from the program for the first compliance period. Staff has proposed an exemption of emissions from waste-to-energy facilities, including modifications to require the retirement of allowances associated with the exempted emissions.

Renewable Energy Credits

Staff proposes clarifications to requirements for the retirement of Renewable Energy Credits (REC’s) to ensure that REC’s are not used to account for zero emissions in multiple programs. Staff has proposed modifications to ensure the retirement requirements are consistently applied to both in-state and out-of-state electrical generation facilities that import electricity to California.
Implementation of Auction and Trading Requirements

Staff has proposed modifications related to the implementation of the auction and trading provisions within the Auction Platform and Compliance Information Tracking Services System (CITSS). Staff also proposed modifications to the current schedule for auctions and reserve sales.

Compliance Obligation Surrender

Staff has proposed requirements and a process for the surrender of compliance instruments for the annual and triennial surrender obligation requirements. These amendments include provisions that specify which instruments are eligible for use, the order of retirement of instruments in the compliance account, and limited future borrowing in cases of allocation true-up.

Compliance Instrument Tracking System Service and Information Disclosure

Staff has proposed modifications to the existing information disclosure requirements and new requirements to ensure rigorous oversight of the market program and of actions taken in the tracking system. Staff has proposed additional information disclosure requirements to help ARB monitor relationships between consultants and market participants.

Market Rules

Staff is proposing modifications to the existing information requirements related to CITSS instrument transfers to aid implementation. These requirements may be used to monitor the market and provide public reports for program transparency. Staff is also proposing modifications to the auction purchase limits.

New Offset Protocol

Staff has proposed to add quantification methodologies for one new proposed Compliance Offset Protocol for mine methane capture projects. A detailed analysis of this protocol is included in Attachment A of the Staff Report.

DETERMINATION OF INCONSISTENCY AND INCOMPATIBILITY WITH EXISTING STATE REGULATIONS

During the process of developing the proposed regulatory action, ARB has conducted a search of any similar regulations on this topic and has concluded that these regulations are neither inconsistent nor incompatible with existing state regulations.
MANDATED BY FEDERAL LAW OR REGULATION

This regulation is not mandated by federal law or regulations.

COMPARABLE FEDERAL REGULATIONS

There are no comparable federal regulations.

AVAILABILITY OF DOCUMENTS AND AGENCY CONTACT PERSONS

ARB staff has prepared a Staff Report: Initial Statement of Reasons (ISOR) for the proposed regulatory action, which includes a summary of the economic and environmental impacts of the proposal. The report is entitled, Staff Report: Initial Statement of Reasons for the Proposed Amendments to the California Cap on Greenhouse Gas Emissions and Market-Based Compliance Mechanisms.

Copies of the ISOR and the full text of the proposed regulatory language, in underline and strikeout format to allow for comparison with the existing regulations, may be accessed on ARB’s website listed below, or may be obtained from the Public Information Office, Air Resources Board, 1001 I Street, Visitors and Environmental Services Center, First Floor, Sacramento, California, 95814, (916) 322-2990, on September 4, 2013.

Final Statement of Reasons Availability

Upon its completion, the Final Statement of Reasons (FSOR) will be available and copies may be requested from the agency contact persons in this notice, or may be accessed on ARB’s website listed below.

Agency Contact Persons

Inquiries concerning the substance of the proposed regulation may be directed to Ms. Rajinder Sahota, Manager of the Climate Change Program Monitoring Section at (916) 323-8503 or Ms. Elizabeth Scheehle, Manager of the Climate Change Program Development Section at (916) 322-7630.

Further, the agency representative and designated back-up contact persons, to whom non substantive inquiries concerning the proposed administrative action may be directed is Ms. Amy Whiting, Regulations Coordinator, at (916) 322-6533. The Board staff has compiled a record for this rulemaking action, which includes all the information upon which the proposal is based. This material is available for inspection upon request to the contact persons.
**Internet Access**

This notice, the ISOR and all subsequent regulatory documents, including the FSOR, when completed, are available on ARB’s website for this rulemaking at [http://www.arb.ca.gov/regact/2013/capandtrade13/capandtrade13.htm](http://www.arb.ca.gov/regact/2013/capandtrade13/capandtrade13.htm)

**DISCLOSURES REGARDING THE PROPOSED REGULATION**

The determinations of the Board’s Executive Officer concerning the costs or savings necessarily incurred by public agencies and private persons and businesses in reasonable compliance with the proposed regulations are presented below.

**Fiscal Impact / Local Mandate**

Pursuant to Government Code sections 11346.5(a)(5) and 11346.5(a)(6), the Executive Officer has determined that the proposed regulatory action would not create costs and may create some savings to covered State agencies. The proposed regulatory action would not create costs or saving in federal funding to the State, costs or mandate to any local agency or school district, whether or not reimbursable by the State pursuant to Government Code, title 2, division 4, part 7 (commencing with section 17500), or other nondiscretionary cost of savings to State or local agencies.

**SIGNIFICANT STATEWIDE ADVERSE ECONOMIC IMPACT DIRECTLY AFFECTING BUSINESS, INCLUDING ABILITY TO COMPETE**

The Executive Officer has made an initial determination that the proposed regulatory action would not have a significant statewide adverse economic impact directly affecting businesses, including the ability of California businesses to compete with businesses in other states, or on representative private persons. In fact, an express purpose of the proposed amendments is to ensure that California businesses’ ability to compete is not directly affected.

**COST IMPACTS ON REPRESENTATIVE PRIVATE PERSONS OR BUSINESSES**

In developing this regulatory proposal, ARB staff evaluated the potential economic impacts to representative private persons or businesses. The ARB is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action.
STATEMENT OF THE RESULTS OF THE ECONOMIC IMPACT ASSESSMENT
PREPARED PURSUANT TO GOVERNMENT CODE SEC. 11346.3(b)

Effect on Jobs/Businesses:

The Executive Officer has determined that the proposed regulatory action would not affect the creation or elimination of jobs within the State of California, the creation of new business or elimination of existing business within the State of California, or the expansion of businesses currently doing business within the State of California. A detailed assessment of the economic impacts of the proposed regulatory action can be found in the ISOR.

Benefits of the Proposed Regulation:

The objective of the proposed amendments to the regulation is to provide additional transition assistance to covered entities, additional cost containment mechanisms and aid in implementation in oversight of the regulation.

A summary of these benefits is provided, please refer to "Objectives and Benefits", under the Informative Digest of Proposed Action and Policy Statement Overview Pursuant to Government Code 11346.5(a)(3) discussion on page 4 of this notice.

A detailed assessment of the economic impacts of the proposed regulatory action can be found in Chapter IV of the ISOR, Economic Impacts of the Proposed Regulation.

EFFECT ON SMALL BUSINESS

The Executive Officer has also determined, pursuant to California Code of Regulation, title 1, section 4, that the proposed regulatory action would not affect small businesses because small businesses in regulated sectors would generally not be subject to the proposed regulation. In general, the total GHG emissions for small businesses are below the GHG reporting threshold, thereby exempting them from compliance obligations under the proposed regulation.

HOUSING COSTS

The Executive Officer has also made the initial determination that the proposed regulatory action will not have a significant effect on housing.
BUSINESS REPORT

In accordance with Government Code sections 11346.3(c) and 11346.5(a)(11), the Executive Officer has found that the reporting requirements of the regulation which apply to businesses are necessary for the health, safety, and welfare of the people of the State of California.

ALTERNATIVES

Before taking final action on the proposed regulatory action, the Board must determine that no reasonable alternative considered by the Board, or that has otherwise been identified and brought to the attention of the Board, would be more effective in carrying out the purpose for which the action is proposed, would be as effective and less burdensome to affected private persons than the proposed action, or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of law.

ENVIRONMENTAL ANALYSIS

In accordance with ARB's certified regulatory program, California Code of Regulations, title 17, sections 60006 through 60007, and the California Environmental Quality Act, Public Resources Code section 21080.5, ARB has conducted an analysis of the potential for significant adverse and beneficial environmental impacts associated with the proposed regulatory action. The environmental analysis of the proposed regulatory action can be found in Chapter III of the ISOR.

WRITTEN COMMENT PERIOD AND SUBMITTAL OF COMMENTS

Interested members of the public may also present comments orally or in writing at the meeting and may provide comments by postal mail or by electronic submittal before the meeting. The public comment period for this regulatory action will begin on September 9, 2013. To be considered by the Board, written comments, not physically submitted at the meeting, must be submitted on or after September 9, 2013 and received no later than 12:00 noon on October 23, 2013, and must be addressed to the following:

Postal mail: Clerk of the Board, Air Resources Board
1001 I Street, Sacramento, California 95814

Electronic submittal: http://www.arb.ca.gov/lispub/comm/bclist.php
You can sign up online in advance to speak at the Board meeting when you submit an electronic board item comment. For more information go to: http://www.arb.ca.gov/board/online-signup.htm.

Please note that under the California Public Records Act (Gov. Code, § 6250 et seq.), your written and oral comments, attachments, and associated contact information (e.g., your address, phone, email, etc.) become part of the public record and can be released to the public upon request.

ARB requests that written and email statements on this item be filed at least 10 days prior to the hearing so that ARB staff and Board members have additional time to consider each comment. The Board encourages members of the public to bring to the attention of staff in advance of the hearing any suggestions for modification of the proposed regulatory action.

Additionally, the Board requests but does not require that persons who submit written comments to the Board reference the title of the proposal in their comments to facilitate review.

**AUTHORITY AND REFERENCE**

This regulatory action is proposed under the authority granted in Health and Safety Code, sections 38510, 38560, 38562, 38564, 38570, 38571, 38580, 39600, 39601, and section 16428.8 Government Code. This action is proposed to implement, interpret, and make specific sections 38530, 38560.5, 38564, 38565, 38570 and 39600 of the Health and Safety Code.

**HEARING PROCEDURES**

The public hearing will be conducted in accordance with the California Administrative Procedure Act, Government Code, title 2, division 3, part 1, chapter 3.5 (commencing with section 11340).

Following the public hearing, the Board may adopt the regulatory language as originally proposed, or with non-substantial or grammatical modifications. The Board may also adopt the proposed regulatory language with other modifications if the text as modified is sufficiently related to the originally proposed text that the public was adequately placed on notice and that the regulatory language as modified could result from the proposed regulatory action; in such event, the full regulatory text, with the modifications clearly indicated, will be made available to the public, for written comment, at least 15-days before it is adopted.
The public may request a copy of the modified regulatory text from ARB's Public Information Office, Air Resources Board, 1001 I Street, Visitors and Environmental Services Center, First Floor, Sacramento, California, 95814, (916) 322-2990.

SPECIAL ACCOMMODATION REQUEST

Consistent with California Government Code Section 7296.2, special accommodation or language needs can be provided for any of the following:

- An interpreter to be available at the hearing;
- Documents made available in an alternate format or another language; or
- A disability-related reasonable accommodation.

To request these special accommodations or language needs, please contact the Clerk of the Board at (916) 322-5594 or by facsimile at 916) 322-3928 as soon as possible, but no later than 10 business days before the scheduled Board hearing. TTY/TDD/Speech to Speech users may dial 711 for the California Relay Service.

Consecuente con la sección 7296.2 del Código de Gobierno de California, una acomodación especial o necesidades lingüísticas pueden ser suministradas para cualquiera de los siguientes:

- Un intérprete que esté disponible en la audiencia
- Documentos disponibles en un formato alterno u otro idioma
- Una acomodación razonable relacionados con una incapacidad

Para solicitar estas comodidades especiales o necesidades de otro idioma, por favor llame a la oficina del Consejo al (916) 322-5594 o envíe un fax a (916) 322-3928 lo más pronto posible, pero no menos de 10 días de trabajo antes del día programado para la audiencia del Consejo. TTY/TDD/Personas que necesiten este servicio pueden marcar el 711 para el Servicio de Retransmisión de Mensajes de California.

CALIFORNIA AIR RESOURCES BOARD

[Signature]

Richard W. Corey
Executive Officer

Date: August 27, 2013